

The Role of the Regulated Sector in the UK Anti-Money Laundering Framework: Pushing the Boundaries of the Private Police

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Abstract

This article argues that the conceptualisation of private police in current academic literature requires expansion to accommodate the role of the regulated sector in the Anti-Money Laundering (AML) framework. Firstly, it evaluates the literature on 'private police' and argues that its current parameters are too narrow to accommodate the 'policing' role of the regulated sector. Secondly, it lays out the legislative framework that has developed to deal with the problem of money laundering. Thirdly, it contextualises the role of the regulated sector, examining the domestic inter-agency policing relationships within the suspicious activity regime as operationalised in Scotland. Finally, it takes a closer look at how the courts have interpreted the 'failure to report offence' under s330 of the Proceeds of Crime Act (POCA) 2002 and its consequential effect on the engagement of the regulated sector with the SARs regime.

Keywords

Money laundering; Policing; Private police; Proceeds of crime

ON 5 MAY 2010, THE CROWN OFFICE AND PROCURATOR FISCAL SERVICE IN SCOTLAND reported that the "[b]iggest ever proceeds of crime case nets \$10 million for Scottish communities". This announcement came at the end of a civil recovery case that was passed to the Civil Recovery Unit in 2008.¹ The Civil Recovery Unit is responsible for the implementation of civil recovery and cash forfeiture in Scotland under Part 5 of the Proceeds of Crime Act 2002. In 2004, Moscow-based businessman Anatoly Kazachkov came to the attention of the police following a Suspicious Activity Report made by a bank within the regulated sector concerning a bank transfer of \$10 million from Hungary to Scotland. The Scottish police, working together with the Russian authorities, were able to trace the source of funds finding evidence of false documentation and stolen identities en route. A restraint order was obtained under the Proceeds of Crime Act 2002. In 2010, following the lengthy court proceedings, the funds were released to the Crown Office.²

This case highlights the vital contribution that the regulated sector can make to policing investigations. However, the academic literature neglects the significant policing role of the regulated sector. Following an exploration of the literature and the legislative

¹ Crown Office & Procurator Fiscal Service (2010). 'Biggest ever proceeds of crime case nets \$10 million for Scottish communities', News release, COPFS, May. Available at <http://www.copfs.gov.uk/News/Latest> (accessed on 17 June 2010).

² *ibid.*

framework, this article seeks to contextualise the policing contribution of the regulated sector within the Anti-Money Laundering (AML) regime as operationalised in Scotland, demonstrating the need for an expansion of the concept of 'private police'.

Private police

The majority of literature which discusses those involved in private policing focuses on the increasing use of private security firms.³ They argue that an increasing number of public, commercial and voluntary bodies are involved in delivering policing services.⁴ For example, privatised spaces (shopping centres, airports, etc.) rely on private security firms to deliver policing services within their boundaries.

Where the literature discusses regulatory roles of private institutions, it tends to fall specifically into the regulatory literature where regulatory responsibilities are examined, as opposed to policing literature which deals with legal, political and social aspects of social control.⁵ Significantly, there has been very little research looking at the role of private forms of regulation in tackling economic crime; rather, it tends to look at health and safety obligations and the environmental regulatory responsibilities.⁶ Where the literature looks at the regulatory responsibilities in the economic crime context, it tends to evaluate the economic burden that is placed on the regulated institutions as opposed to their active policing contributions.⁷

Harvey focuses on the costs incurred by the regulated sector in complying with its obligations.⁸ She analyses how much it costs for the regulated sector to implement the required measures at length. She recognises that there is a gap in the academic literature for work quantifying 'benefit' to society. However, she does not undertake this task. Furthermore, while she acknowledges that the regulated sector considers that they are "unpaid policemen" and that they have "inside knowledge", she does not explore this policing role nor appreciate its significance. It is important because the regulated sector is in a position to connect the public police to transactional information at an earlier stage in the commission of money laundering. Sproat has criticised Harvey's methodology.⁹ He analyses costs from both the regulated sector and the public sector perspectives and

³ Loader, I. (1999) 'Consumer Culture and the Commodification of Policing and Security', *Sociology*, 33, pp. 373-392; Brodeur, J.P. and Shearing, C. (2005). 'Configuring Security and Justice', *European Journal of Criminology*, 2 (4), pp. 379-406; Crawford, A., Lister, S., Blackburn, S. and Burnett, J. (2005). *Plural Policing: The Mixed Economy of Visible Patrols in England and Wales*, Bristol: Policy Press; Crawford, A. (2006). 'Networked Governance and the Post-regulatory State?: Steering, Rowing and Anchoring the Provision of Policing and Security', *Theoretical Criminology*, 10, pp. 449-479; Vaughan, B. (2007). 'The Provision of Policing and the Problem of Pluralism', *Theoretical Criminology*, 11, pp. 347-363; Johnston, L. (2007). 'The Trajectory of 'Private Policing'', in Henry, A. and Smith, D., *Transformations of Policing*, Aldershot: Ashgate, pp. 25-49.

⁴ Loader, I. (1999) 'Consumer Culture and the Commodification of Policing and Security', *Sociology*, 33, pp. 373-392.

⁵ Shearing, C. D. (1993). 'A Constitutive Conception of Regulation', in Grabosky, P and Braithwaite, J (eds), *Business Regulation and Australia's Future*, Canberra: Australian Institute of Criminology; Gill, P. (2002). 'Policing and Regulation: What is the Difference?' *Social Legal Studies*, 11, pp. 523-546.

⁶ Williams, J. (2005). 'Reflections on the Private versus Public Policing of Economic Crime', *Brit.J.Criminol*, 45, pp. 316-336 at p317. For an environmental example, see Abbot, C. (2009). 'The Regulatory Enforcement and Sanctions Act 2008', *Env L Rev*, 11(1), pp. 38-45, which looks at the role of Local Authorities in enforcing environmental health obligations.

⁷ Harvey, J. (2004). 'Compliance and Reporting Issues Arising for Financial Institutions from Money Laundering Regulations: A Preliminary Cost Benefit Study', *Journal of Money Laundering Control*, 7(4), pp. 333-346; Harvey, J. (2005). 'An Evaluation of Money Laundering Policies', *Journal of Money Laundering Control*, 8 (4), pp. 339-345; Sproat, P. (2007). 'The New Policing of Assets and the New Assets of Policing: A Tentative Financial Cost-benefit Analysis of the UK's Anti-money Laundering and Asset Recovery Regime', *Journal of Money Laundering Control*, 10 (3), pp. 277-299.

⁸ *ibid.*

⁹ Sproat, n7 above.

acknowledges where the data is merely indicative or secondary, and in this respect insulates his methodology from critique. He goes on to attempt to analyse the 'benefit', but concludes that the regime is still bedding down. In his later work, Sproat spends more time quantifying the benefits of the AML framework.¹⁰ Through a myriad of methodological disclaimers, he finds that the system does not pay for itself. The analysis does not attempt to provide a qualitative appraisal of the 'benefit'. Sproat argues that those who support the AML framework are likely to argue that 'benefit' extends beyond the costs and into the realms of punitive rewards. Neither Harvey nor Sproat highlight the material contribution that the regulated sector is able to make to the policing of money laundering. Similarly, they do not acknowledge the position of power in which the regulated sector is, given its access to customer/client information.

Sheptycki defines private policing simply as "contract based" policing.¹¹ However, it is argued here that this interpretation is too narrow and that the AML framework has imposed on the regulated sector legislative responsibilities of a policing character. Academic literature must bring policing and regulation together since the AML obligations placed on the regulated sector means that its members enter into the policing arena and play a fundamental role in supporting the public police in their investigations. These obligations move the regulated sector from a simple compliance role into that of private police.

The problem of money laundering

The first articulation of a collective 'money laundering' concept appeared in the 1988 United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances. Money laundering was initially perceived as mainly linked to drug-trafficking. Through discussions at the G7 summit in 1989, when the Financial Action Task Force (FATF) was established, its conceptualisation as a threat to the international economy came to the fore.¹² Money laundering was acknowledged as a major global threat to the financial markets. The establishment of the FATF harnessed the commitment of 16 members (which included the European Commission) to band together in their attempts to draft national and international policies tackling money laundering.¹³

The remit of FATF laid down in its 2008-2012 revised mandate is to work to ensure that its 40 Recommendations on Money Laundering and nine Recommendations on Terrorist Financing are recognised globally.¹⁴ FATF will continue to focus on three main areas of activity; standard setting, ensuring effective compliance with those standards and identifying money laundering and terrorist financing threats. FATF highlights jurisdictions that have significant deficiencies in their AML and combating financing of terrorism regimes, and these are to be categorised as 'high-risk jurisdictions'. FATF will identify systemic money laundering and terrorist financing threats through the typologies process

¹⁰ Sproat, P. (2009). 'To What Extent is the UK's Anti-money Laundering and Asset Recovery Regime Used against Organised Crime?', *Journal of Money Laundering Control*, 12 (2), pp. 134-150; Sproat, P. (2009). 'Payback Time? To What Extent has the New Policing of Assets Provided New Assets for Policing?', *Journal of Money Laundering Control*, 12 (4), pp. 392-405

¹¹ Sheptycki, J. (2002). 'Accountability Across the Policing Field: Towards a General Cartography of Accountability for Post-modern Policing', *Policing & Society*, Special Issue on Police Accountability in Europe (Guest Editor Monica den Boer), 12 (4), pp. 323-338.

¹² Contained in the Economic Declaration Released by the Summit of the Arch, July 16, 1989. Also see Mitsilegas, V. and Gilmore, B. (2007). 'The EU Legislative Framework against Money Laundering and Terrorist Finance: A Critical Analysis in the Light of Evolving Global Standards', *J.C.L.Q.*, 56 (1), pp. 119-140.

¹³ This membership has now increased to 34 members. See http://www.fatf-gafi.org/pages/0,3417,en_32250379_32236836_1_1_1_1_1,00.html (accessed 18 June 2010).

¹⁴ Initially, the FATF drafted 40 Recommendations which dealt with money laundering. In 2001, the remit of the FATF was expanded to include tackling terrorist financing; consequently, they drafted 8 further Recommendations. In 2003, the FATF revised all Recommendations and added a 9th Recommendation.

where they gather and disseminate information on methods, trends and techniques. FATF will support the development of national threat assessments and will regularly publish a global threat assessment. Lastly, and perhaps most significantly, FATF will look to new emerging threats. It acknowledges that globalisation brings with it new risks and the central consideration internationally must be to protect the integrity of the financial system. Looking to their 40 Recommendations, 'risk' terminology permeates, yet there is no definition or interpretative guidance given in the document. From June 2007 to October 2009 (and presumably to be periodically revised), FATF issued separate guidance on the risk-based approach which was sector specific. The guidance aims to:

- 1) Support the development of a common understanding of what the risk-based approach involves.
- 2) Outline the high-level principles involved in applying the risk-based approach.
- 3) Indicate good practice in the design and implementation of an effective risk-based approach.¹⁵

Countries which are seeking to institute an appropriate risk-based system must understand the risk that they are tackling. They must have information available to them that allows them to assess the risk appropriately or, in other words, "they must understand the actual and potential money laundering and terrorist financing risk."¹⁶

The participation of the European Commission, together with numerous Member States in the FATF, helped to push forward legislative provisions in the European Communities (now EU). In 1991, building on the FATF 40 Recommendations which were first published in 1990, the European Union produced the First Money Laundering Directive on prevention of the use of the financial system for the purpose of money laundering¹⁷. Ten years later, in 2001 the Second Money Laundering Directive was introduced.¹⁸ This Directive extended the offences covered by the First Directive, extended the range of professions covered and established the requirement for the establishment of a Financial Intelligent Unit within each Member State who would be responsible for administering the suspicious activity regime. The Third Money Laundering Directive was issued in 2005 and came into force in 2007¹⁹. It incorporated the 2003 revisions of the FATF Recommendations, extended the scope of the Directive to cover any transaction linked to terrorist financing, instituted customer due diligence measures, enhanced diligence measures in respect of politically exposed persons and established penalties for failing to report suspicious activity.

The Proceeds of Crime Act (POCA) 2002, together with the Money Laundering Regulations of 2007, lays down the criminal and regulatory sanctions that deal with money laundering transposing the European provisions into the UK framework. They determine what activities are included in the crime of 'money laundering' and the consequential provisions that facilitate its investigation and prosecution. The POCA 2002 Explanatory Notes (at n6) describe money laundering as "the process by which the proceeds of crime are converted into assets which appear to have legitimate origin." In other words some kind of criminal activity has taken place which has resulted in a material benefit. To ensure this benefit can be used without detection by law enforcement authorities, it must be disguised in such a way that it is no longer connected to its original source. In achieving untraceable funds, those businesses which deal with financial interests are the most at risk of exploitation. The

¹⁵ Paraphrased from the FATF website, available at http://www.fatf-gafi.org/document/63/0,3343,en_32250379_32236920_44513535_1_1_1_1,00.html (accessed on 17 June 2010).

¹⁶ De Koker, L. (2009). 'Identifying and Managing Low Money Laundering Risk: Perspectives on FATF's Risk-based Guidance', *Journal of Financial Crime*, 16 (4), pp. 334-352 at p. 337.

¹⁷ 91/308/EEC

¹⁸ 2001/97/EC

¹⁹ 2005/60/EC

association between money laundering and low level criminality through serious organised crime, taken together with the potential risk to the economy, moved anti-money laundering procedures up the political agenda.

Moves to highlight how money laundering relates to criminality, with an emphasis placed on how much it impacts daily life, have been embraced by both policing and political bodies in an attempt to harness the necessary public support to drive forward criminalisation. For example, the UK Threat Assessment of Organised Crime (2009/10) published by the Serious Organised Crime Agency (SOCA), highlights the link between money laundering and organised crime explaining that “most organised criminal activity is directly or indirectly aimed at making money and therefore criminal finances and profits underpin organised crime.”²⁰ Similarly, “Letting Our Communities Flourish: A Strategy for Tackling Organised Crime in Scotland” published by the Scottish Government in 2009 was at pains to highlight how far the tentacles of organised crime reach and emphasised criminals’ reliance on money laundering activities to sustain their empires. The breadth of criminal activity and the variety of environments exploited by criminals has forced the traditional public police to diversify and pluralise, thereby embracing the regulated sector.

The public police and the regulated sector

Reiner argues that “anyone living in modern society has this intuitive notion of what the police are”.²¹ However, when one tries to articulate a definition of the police, the debate is not so much concerned with what the police are, as it is with what they do – be that what they actually do, or what they should do.²² The definitions narrated here are focused on facilitating an understanding of the role that the public police play in the AML framework so that this can be contrasted and reconciled with the role of the private police.

The public police are organisations established in connection with the state to assist in the maintenance of order and the prevention of crime.²³ In relation to AML in particular, there are a number of policing agencies involved in the implementation and enforcement of the UK framework. They appear on the surface to be hierarchical. However, their roles overlap and intertwine as they attempt to snare money launderers. These roles and responsibilities ‘in action’ demonstrate that despite the inter-dependence of policing agencies, there remains a definitive line between the private and public police. The current portrayal of the private police in academic literature does not accommodate the role of the regulated sector or professional bodies (in their capacity as supervisory authorities) in the AML framework.

In Scotland, responsibility for law and order generally lies with the Scottish Executive and Scottish Parliament under The Police (Scotland) Act 1967. However, certain matters are reserved to the UK Parliament at Westminster, including national security, terrorism, firearms, drugs and specifically the financial markets and money laundering as detailed in The Scotland Act 1998 Schedule 5. Consequently, the policing arrangements in respect of AML operations in Scotland are administered on the basis of UK wide legislation.²⁴

²⁰ SOCA. (2010). ‘The UK Threat Assessment of Organised Crime 2009/10’, p. 8. Available at <http://www.soca.gov.uk/threats>.

²¹ Reiner, R. (2000). *The Politics of the Police*. Oxford: Oxford University Press, UK, 3rd Ed., p. 1.

²² Bayley, D. H. (2005). ‘What Do the Police Do?’, in T. Newburn (ed.), *Police: Key Readings*. Cullompton: Willan, pp. 141-148.

²³ Sheptycki, n11 above; Reiner, n21 above.

²⁴ It should be noted that moves are being made to try and devolve the policing of drugs detailed in ‘Letting Our Communities Flourish - One Year On: A Strategy for Tackling Organised Crime in Scotland’ published by the Scottish Government in 2010.

The most significant policing agency within the UK AML framework is the Serious Organised Crime Agency (SOCA). SOCA was set up under the Serious Organised Crime and Police Act 2005 (SOCPA 2005). SOCA is a hybrid agency, which subsumed the National Crime Squad and the National Criminal Intelligence Service and in addition, certain responsibilities of Her Majesty's Revenue and Customs (HMRC) in relation to drug trafficking, and Her Majesty's Immigration Service (HMIS) in relation to human trafficking.²⁵ SOCA is significant because it contains the UK Financial Intelligence Unit (UK FIU) which is responsible for administering the suspicious activity regime across the whole of the UK. As noted above, the Third Money Laundering Directive laid down a requirement on Member States to establish a national Financial Intelligence Unit (FIU), if they had not already done so. To all intents and purposes, the UK had a national financial intelligence unit in the form of the Financial Intelligence Division of the National Criminal Intelligence Service (NCIS). However, when SOCA was established in 2006, it took over the responsibilities of NCIS and consequently the UK FIU.²⁶ In accordance with Article 29 of the Third Money Laundering Directive, which determined that a national FIU should be responsible for collecting, analysing, and disseminating suspicious transactions reports, SOCA is now responsible for administering the UK Suspicious Activity Reports (SARs) regime.

Section 2 SOCPA 2005 lays down SOCA's functions to include the prevention and detection of serious organised crime and to contribute to its reduction and the mitigation of its consequences. Its functions are expanded further into the realm of crime in general under section 3. Neither 'serious organised crime' nor 'crime' is defined in the Act. Nevertheless, it does lay down a requirement for the Secretary of State to set strategic priorities (in consultation with SOCA and Scottish Ministers), and under s61 there is a list of offences which fall within SOCA's remit, including but not limited to, those specified in Schedule 4 POCA 2002 Lifestyle offences: Scotland. Taken together, these provide some guidance as to what is considered serious organised crime and crime more generally of interest to SOCA. Although SOCA is a key player in the UK AML framework as a whole, it has particular restrictions placed on how it interacts with the Scottish public police. In terms of section 22 SOCPA 2005, SOCA can only carry out activities in Scotland in relation to an offence which it suspects has, or is being, committed, if it has the agreement of the Lord Advocate. Indeed, despite SOCA being established in 2006, SOCA's 2010-2011 Annual Plan narrates the first stand-alone investigation in Scotland which took place over the course of 2009 and 2010.²⁷

In Scotland, there are eight territorial public police forces, which cover different geographical areas.²⁸ Within each territorial force, there is a Financial Intelligence Unit (FIU), and this department deals most closely with anti-money laundering. In addition, there is the Scottish Drug Enforcement Agency (SDEA), which was established in April 2001. SDEA was renamed the Scottish Crime and Drug Enforcement Agency (SCDEA) by the Police, Public Order and Criminal Justice (Scotland) Act in 2006. SCDEA's functions are laid down in section 2(2) as: preventing and detecting serious organised crime; contributing to the reduction of such crime in other ways and to the mitigation of its consequences; and gathering, storing and analysing information relevant to the prevention, detection, investigation or prosecution of offences; or the reduction of crime

²⁵ Harfield, C. (2006). 'SOCA: A Paradigm Shift in British Policing', *Brit. J. Criminol*, 46, pp. 743-761; Fitzpatrick, D. (2005). 'Advising the Serious Organised Crime Agency: The Role of the Specialist Prosecutors', *Journal of Financial Crime*, 12 (3), pp. 251-263; Fitzpatrick, D. (2006). 'Crime Fighting in the Twenty-first Century? A Practitioner's Assessment of the Serious Organised Crime and Police Act 2005', *Journal of Money Laundering Control*, 9 (2), pp. 129-140; Leong, A. (2007). 'Anti-money Laundering Measures in the UK: A Review of Recent Legislation and FSA's Risk-based Approach', *Co. Law*, 28 (2), pp. 35-42.

²⁶ International Monetary Fund. (2004). 'Financial intelligence Units: An Overview', Washington D.C., p. 29.

²⁷ SOCA Annual Plan 2010-2011, p. 14.

²⁸ Donnelly, D. and Scott, K. (2005). *Policing Scotland*. Cullompton: Willan.

in other ways or the mitigation of its consequences.²⁹ This provision mirrors the remit of SOCA. SCDEA's strategic priorities are laid down by the Scottish Government under section 13 and are disseminated through SCDEA's Annual Plan in accordance with section 14. The 2010-2011 Annual Plan (which forms part of a larger five-year Strategic Plan 2010-2015) details their priorities to include: the identification of criminal assets for restraint under the Proceeds of Crime Act 2002; to make it more difficult for serious organised crime groups to obtain the *services of specialists* to protect and launder illegal gains, and specifically to engage with the *business sector* and assist *legitimate businesses* in protecting themselves from serious organised crime [emphasis added]. Following two reports issued in 2000, the HM Inspectorate of Constabulary Report on the Confiscation of Criminal Assets in Scotland "Making Crime Pay" and "Recovering the Proceeds of Crime" Report by the UK Cabinet Office's Performance and Innovation Unit, the Association of Chief Police Officers of Scotland (ACPOS) Crime Standing Committee set up a Multi-Agency Working Group to consider the issues raised. The reports highlighted that financial investigation was being sidelined both in respect of resourcing and usage. Reflecting on the reports, the Multi-Agency Working Group concluded that the way forward was the establishment of a Scottish Multi-Agency Financial Investigation Unit/Money laundering Unit.³⁰ Consequently, in September 2001 the Scottish Money Laundering Unit (SMLU) was established within SCDEA.

The SMLU contains staff from SCDEA, HMRC, and the Department of Work and Pensions (DWP). Its functions are to identify assets gained through illegal activity, such as drug trafficking and serious and organised crime, and to make these assets available to the courts for confiscation, to target those involved in laundering criminal assets, to provide high quality financial intelligence, to service the needs of SDEA (which became SCDEA) Operations and Intelligence Groups, and to provide assistance to Scottish Police forces in respect of financial investigation.³¹ Subsequently, the SMLU became the single point of contact for the Scottish police service in the administration of suspicious financial activity disclosed to SOCA by institutions within the regulated sector.³² While there is a striking similarity with the functions of SOCA, it is intended that SOCA and SCDEA engage in partnership rather than duplication, and this is borne out operationally through a Partnership Agreement between the agencies.³³ SOCPA 2005 sections 23 to 25 lay down a number of provisions which provide a legislative basis for such agreements. This mutual assistance can be at the request of either agency. These provisions are not limited to these two agencies and would provide a legislative basis for any Scottish force to request assistance (or to be approached for assistance by SOCA).

There are additional public police forces, such as the Civil Nuclear Constabulary and the British Transport Police, that have a UK wide jurisdiction and consequently play a role in Scottish policing. Moreover, the Security Service, MI5, works with SOCA in tackling serious crime. SOCPA 2005 amended the Security Services Act 1989 to clarify the role of MI5, specifying that MI5 should act in support of the activities of SOCA. It is difficult to assess how this relationship functions since both MI5 and SOCA are, due the sensitivity of their areas of work, not subject to the Freedom of Information Act 2000 or its counterpart the Freedom of Information (Scotland) Act 2002, and as far as we can ascertain there is no academic literature on the subject. Similarly, MI6, the UK's external intelligence service, could potentially police in the anti-money laundering arena, since they are mandated under the Intelligence Services Act 1994 section 1 to act in support of the prevention or detection of serious crime. While acknowledging that both MI5 and MI6 may have a role in

²⁹ Paraphrased from s2(2) Police, Public Order and Criminal Justice (Scotland) Act 2006.

³⁰ SDEA Annual Report 2000-2001, p. 15.

³¹ SDEA Annual Report 2001-2002, p. 18.

³² SDEA Annual Report 2002-2003, p. 9.

³³ SCDEA Annual Report 2005-2006, p. 7.

the overarching policing of money laundering, the focus of this article is on the public/private policing nexus. This is best illustrated by focusing on the SARs regime, and in this respect as these agencies do not have a direct role they will be put to one side.

The private police involved in the AML framework are those who fall within the regulated sector detailed in POCA 2002 Schedule 9 Part 1, including banking institutions, businesses providing investment services, accountants, tax advisors, estate agents, auctioneers, casinos and many more. Straddling the gap between the public and private police in this arena are those defined as “supervisory authorities” under Reg. 23 Money Laundering Regulations (MLR) 2007 and “designated authority” under Reg. 36. Supervisory authorities laid down in Reg. 23 include the Financial Services Authority, the Office of Fair Trading, professional bodies (listed in Schedule 3 MLR 2007), the Commissioners of HMRC, the Gambling Commission, the Department of Enterprise, Trade and Investment (DETI) of Northern Ireland and the Secretary of State who is the designated supervisory authority for insolvency practitioners authorised by him under section 393 of the Insolvency Act 1986. Of these supervisory authorities, the FSA, OFT, HMRC and DETI are also designated authorities under Reg. 36.³⁴

Reg. 24 sets out that it is the responsibility of the supervisory authority to monitor supervisees. The supervisory authority must take appropriate measures to secure their compliance and, where it comes to the attention of the supervisor that a person may have engaged in money laundering, they must report this to SOCA. The remit of designated authorities goes further. They are given more specific enforcement powers under Part 5 including: the power to require information (Reg. 37), power of entry without a warrant (in limited circumstances under Reg. 38), and power to enter premises with a warrant (Reg. 39). All designated authorities have the power to impose civil penalties where certain regulations have not been complied with under Reg. 42. All violations liable to civil penalties under Reg. 42 are also criminal offences in terms of Reg. 45, with the minor exception of Reg. 11(1d), which requires “a relevant person to consider whether he is required to make a disclosure under Part 7 of the Proceeds of Crime Act 2002 or Part 3 of the Terrorism Act 2000”. Presumably, this has not been made a criminal offence since to prove or disprove consideration would be extremely difficult and the issue can be adequately dealt with through the civil penalties under Reg. 42. Reg 46 sets out that the designated authorities, with the exception of the FSA, are able to institute prosecution proceedings in England, Wales and Northern Ireland. However, they do not have jurisdiction in Scotland. It is for the Procurator Fiscal within the Crown Office and Procurator Fiscal Service to decide whether to proceed with a prosecution in Scotland.

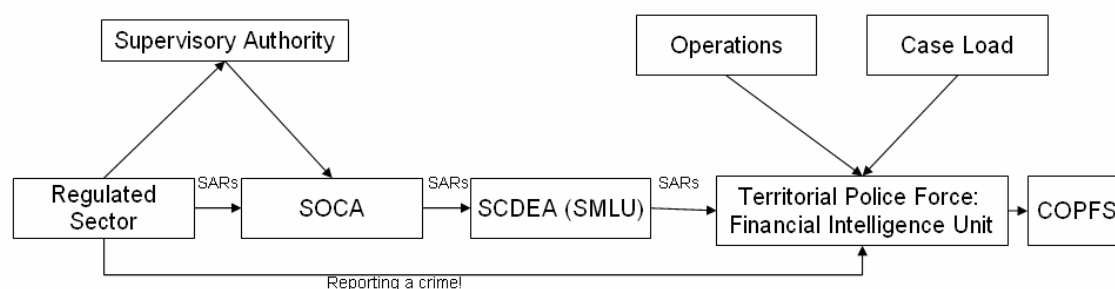
It appears that the majority of these authorities, supervisory or designated, fall within the definition of public police. They are established in connection with the state and following the provisions of MLR 2007 and POCA 2002 have been placed in a role which entails the maintenance of order and the prevention of crime. For example, the FSA was established by the Financial Services and Markets Act (FSMA) 2000. While theoretically an independent body receiving no government funding, their objectives have been set by FSMA 2000, specifically including reducing the extent to which it is possible for a business to be used for a purpose connected with financial crime. Similarly, HMRC was established by the Commissioners for Revenue and Customs Act 2005. HMRC subsumed the functions of the Inland Revenue and Customs and Excise under s5 of the 2005 Act. In exercising these functions, HMRC are in the position of gathering information which could potentially lead to the discovery of criminal activity ranging from fraud and tax evasion to money laundering. Furthermore, through their responsibilities and powers given by both POCA

³⁴ Hynes, P. Furlong, R. and Rudolf, N. (2009), *International Money Laundering and Terrorist Financing: A UK Perspective*. London: Sweet and Maxwell, p. 26.

2002 and MLR 2007, they are in a position to investigate and prosecute in England, Wales, and Northern Ireland. Although, as noted above, they would have to refer matters to the Crown Office and Procurator Fiscal Service in Scotland.³⁵ However, it is worthy of note that the professional bodies listed in Sch. 3 that fall into the category of supervisory authorities, vary in modes of establishment, funding arrangements and accountability.³⁶ Unfortunately, further examination of these 22 institutions is beyond the scope of this article. Figure 1 provides a visual representation of how the public police and regulated sector interact in the SARs regime.

Figure 1: Basic UK AML structure

Figure drawn by the author on the basis of the relevant legislative provisions and the SCDEA annual reports



Key

Regulated Sector = Schedule 9 Part 1, POCA 2002
 SOCA = Serious Organised Crime Agency
 Supervisory Authority = Reg 23 MLR 2007 & Sch 9 Part 2 POCA 2002
 SCDEA = Scottish Crime and Drug Enforcement Agency
 SMLU = Scottish Money Laundering Unit
 Territorial Police Force = Any of the 8 Scottish Police Forces
 COPFS = Crown Office and Procurator Fiscal Service
 Operations = policing 'projects' involving multiple policing departments concerning targets/activities selected by the Chief Constable
 Case Load = cases which are ongoing (eg profile going back and forth with PF)
 SARs = Suspicious Activity Reports

The regulated sector has a duty to report any activity where it is suspected that an individual is engaged in money laundering.³⁷ SARs are passed internally to the nominated officer, universally referred to as the Money Laundering Reporting Officer (MLRO), who is obliged to determine whether it is required to make a report. If the MLRO is satisfied that a report requires to be made, it is made to the SOCA. An individual can also report directly to a person authorised for such purposes by the Director General of SOCA. Also, where suspicion is raised in relation to a particular transaction, the regulated sector has a duty to seek consent before proceeding.³⁸ Once the initial request for consent has been made, the hands of the regulated institution are tied. Consent can be inferred when the period of

³⁵ POCA 2002, s2C and MLR 2007, Reg. 46.

³⁶ The professional bodies listed in MLR 2007 Sch. 3 correspond to those listed in POCA 2002 Sch. 9 Part 2.

³⁷ POCA 2002 s330.

³⁸ POCA 2002 s327, s328 and s329.

seven days has passed since the report was made and no notice of refusal has been received.³⁹ Where the reporting institution receives notice that consent is refused, they will be able to act once a moratorium period of 31 days has passed. SOCA collates relevant SARs which are accessible through a database window by territorial forces.⁴⁰ The territorial forces can view SARs that have been allocated to them by SOCA. In addition, the SCDEA (SMLU) can see SARs allocated to all the Scottish territorial forces. SCDEA will sift these reports and run further checks to identify those of most interest. It has been estimated that SCDEA receives about 8,000 SARs per year.⁴¹ They put together parcels of the information they have collected and highlight the relevant reports to the appropriate territorial FIU. The FIU then decides whether or not the SAR requires action or provides intelligence of such significance as to warrant entry on the Scottish Intelligence Database (SID). Increasing the amount of intelligence that can be taken from a SAR is a key priority of SOCA identified in Part 3 of their SARs Annual Report 2009. 'Intelligence' here is a piece of information which has been interpreted and analysed as potentially relevant to an investigation of criminal activity and consequently may inform future action.⁴² The SID database is accessible by all Scottish territorial forces.

FIUs will have ongoing caseloads where they are trying to compile (or refine) financial profiles intending to seek restraint or confiscation. In doing this, they may have to call upon the regulated sector to supply further information. If the regulated sector refuses to disclose the information, the FIU can have recourse to the investigatory powers available under Part 8 POCA 2002. Chapter 3 deals with the Scottish provisions, which include production orders and search warrants, and, of more significance to the regulated sector, customer information orders and account monitoring orders. While maintaining their own caseload, FIUs participate in ongoing force operations. These are projects that involve multiple policing departments. They focus on specific targets or activities that are selected by the Chief Constable.⁴³ The officer in charge of a particular operation would contact the FIU to see what intelligence they are able to contribute. Mainstreaming financial intelligence within force operations facilitates identification of assets for restraint at an earlier stage and is of increasing importance in implementing POCA 2002.⁴⁴ In effect, the FIU looks at SID in a new light. This new focus may draw their attention to a previously unassuming SAR. The operation has made the SAR of more significance and it may be appropriate for the FIU to investigate the SAR anew, again approaching the regulated sector for further information.

The public police in Scotland have invested in the development of their FIUs with the support of the Scottish Government as part of "Letting Our Communities Flourish: A Strategy for Tackling Organised Crime in Scotland" noted earlier. Lothian and Borders, Tayside and Strathclyde police forces received a share of the money that has been recovered from criminals. This money has been used to recruit 19 financial investigators. The individual police forces had to decide whether to recruit police officers or civilian financial investigators. In making their decision they will have been conscious of the constant pressure to provide 'best value'⁴⁵ while adopting effective strategies to tackle

³⁹ POCA 2002 s335(2).

⁴⁰ Leong, A. n25 above.

⁴¹ HM Inspectorate of Constabulary for Scotland (HMICS) and the Inspectorate of Prosecution in Scotland (IPS). (2009). Joint Thematic Report on the Proceeds of Crime Act 2002, p. 34.

⁴² Innes, M, Fielding, N. and Cope, N. (2005). 'The Appliance of Science?' The Theory and Practice of Crime intelligence Analysis', *Brit. J. Criminol*, 45 (1) pp. 37-57.

⁴³ Donnelly, D. and Scott, K. n28 above, p. 17.

⁴⁴ HMICS & IPS. (2009). Joint Thematic Report on the Proceeds of Crime Act 2002, p. 23; Murray, K. (2010). 'Dismantling Organised Crime Groups Through Enforcement of the POCA Money Laundering Offences', *Journal of Money Laundering Control*, 13 (1), pp. 7-14.

⁴⁵ Although the concept of 'best value' first originated under the Labour government in an attempt to sweep away the competitive compulsory tender that had been adopted by the Conservative government and geared towards Councils, it has now become firmly entrenched in public police management. See Martin, S. (2000).

money laundering. The ability of the FIUs to influence operational and strategic choices depends on their internal authority structure and how it is impacted by the acknowledged command and control structure of the public police.⁴⁶ Civilian staff are at the bottom of the internal authority structure; consequently, increasing the number of civilian staff is unlikely to improve the ability of the FIUs to influence operational or strategic choices. There are limits on the role civilian staff are able to play within FIUs. Civilian staff in Scotland cannot execute investigative orders, such as production orders or search warrants, since this requires a police officer.⁴⁷ Nevertheless, civilian staff provide a cheaper alternative to police officers. In addition, as they often come from external agencies, frequently as members of the regulated sector, they are trained in specialist skills such as accounting and insolvency, which is of particular assistance. Moreover, their experience in the regulated sector means that they bring with them the ability to understand the burden placed on the regulated sector and are able to foster relationships of trust. Rhodes argues that in the field of policing it is the “shared values and norms [that] are the glue which holds the complex set of relationships together; trust is essential for co-operative behaviour”.⁴⁸ This is particularly crucial given the sensitive nature of the material that is shared between the public and private police in their attempts to tackle money laundering. Such knowledge exchange is also available to the regulated sector through the recruitment of ex-police officers as compliance officers, and this has been found to be advantageous in fostering relationships of trust between public and private institutions.⁴⁹

In addition to reporting responsibilities under POCA 2002, the regulated sector has obligations under MLR 2007. Reg. 5 requires that those in the regulated sector undertake customer due diligence measures which are known as the ‘know your client’ obligations. They have a duty to verify the identity of customers or beneficial owners and also to be aware of the nature of their clients’ business. They must monitor this relationship on an ongoing basis (Reg. 8). The obligation is geared towards enabling members of the regulated sector to spot transactions which are out of the ordinary and thereby placing them in a position where they have a duty to report.⁵⁰ Moreover, under Part 3, they must keep records of this information, adopt appropriate procedures and train their staff. In fulfilling these regulations, the regulated sector undertakes crucial collection of intelligence, and they are responsible for connecting this intelligence to the public police through their use of SARs. Does the access of the regulated sector to customer/client information (which may later prove to have intelligence value) shift the balance of power from the state to the regulated sector? SARs put them in a position to materially control

Implementing ‘Best Value’: Local Public Services in Transition’, *Public Administration*, 78 (1), pp. 209–227. This is evidenced both north and south of the border in the Scottish Policing Performance Framework and ACPOS National Procurement Strategy.

⁴⁶ HMICS & IPS, n44 above, p. 14. It is for the Chief Constable to make operational decisions taking on board the pressures on available resources. In making such decisions, the Chief Constable will receive advice from senior officers. It was acknowledged in the HMICS & IPS report that FIUs in Scotland do not have the requisite representation to highlight the potential of the department and secure appropriate resources. However, with the recent appointment of ACPOS Proceeds of Crime Champions this is likely to improve. The role of the ACPOS Champions is to mainstream the use of POCA 2002. As it is the FIU who currently have the most expertise, it is likely they will be instrumental in supporting the ACPOS Champions. See ‘New POCA ‘Champions’ to disrupt serious and organised crime’ COPFS Press Release. Available at: <http://www.copfs.gov.uk/News/Releases/2010/03/30103126> (accessed on 20 June 2010).

⁴⁷ Investigative Orders under the Proceeds of Crime Act 2002, Code of Practice Issued under s410 of the Proceeds of Crime Act 2002.

⁴⁸ Rhodes, R.A.W. (2007). ‘Understanding Governance: Ten Years On’, *Organization Studies*, 28 (8), pp. 1243–1264 at p1246.

⁴⁹ Verhage, A. (2009a). ‘Compliance and AML in Belgium: A Booming Sector with Growing Pains’, *Journal of Money Laundering Control*, 12 (2), pp. 113–133; Verhage, A. (2009b). ‘The Anti Money Laundering Complex: Power Pantomime or Potential Playoff?’, in J. Shapland and P. Ponsaers (eds), *The Informal Economy and Connections with Organised Crime*. The Hague: BJU Legal Publishers; Favarel-Garrigues, G., Godefroy, T. and Lascoumes, P. (2008). ‘Sentinels in the Banking Industry: Private Actors and the Fight against Money Laundering in France’, *Brit. J. Criminol*, 48 (1), pp. 1–19.

⁵⁰ Harvey, J. n7 above; Leong, A. n25 above.

their policing contribution. S330(2) POCA 2002 accommodates a subjective test of 'suspicion'; consequently, they can choose whether or not to make a SAR. In deciding what constitutes suspicious activity, they are effectively deciding what should be brought to the attention of the state and what should remain a private matter.⁵¹ They are able to balance the interests of the state against private interests.

There are two prongs to the private interests of the regulated sector: those of the institution itself and those of its clients and customers. Each influences the engagement of the regulated sector with the AML regime in the UK. As highlighted previously, where suspicion has been raised in relation to a particular transaction, members of the regulated sector have a duty to seek consent before proceeding.⁵² While they may be called upon to justify their actions to clients, they must be wary lest they fall foul of the "tipping off" offence and face criminal sanctions.⁵³ The precariousness of the position of the regulated sector has been exacerbated by the recent English civil case of *Shah v HSBC Private Bank Ltd*.⁵⁴ In this case Mr Shah, along with his wife, sought damages from HSBC for their failure to carry out transactions in accordance with his instructions, breaching their duty towards them. Several transactions were instructed by Mr Shah at different intervals. These transactions were placed on hold while HSBC complied with their statutory obligations. A number of disclosures were made and responded to by SOCA. There were four transactions in total in respect to which HSBC refused to act until they had received consent. Mr Shah claimed that the effective freezing of the Shahs' assets caused a cascade of events resulting in the Reserve Bank of Zimbabwe seizing his assets over which they had control, totalling \$307.5million. HSBCs mounted a defence claiming that they had suspected that the transactions constituted money laundering, and consequently as they had made an authorised disclosure in accordance with s338 POCA 2002, they were unable to act earlier than they did because to do so would be illegal. The action proceeded to a summary judgement, which found in favour of HSBC on the grounds that since Mr Shah was not challenging the good faith of the bank, there was no real prospect of Mr Shah establishing that there had been a breach of duty by the bank. Mr Shah appealed on this basis that his claim should not have been dismissed at such an early juncture.

Mr Shah's case was largely based on the fact that HSBC had failed to carry out his instructions promptly and that, in raising the defence that they suspected Mr Shah of being involved in money laundering, they should be required to adduce evidence of their suspicion. In affirming *R v Da Silva*,⁵⁵ the Court found that, while there is no requirement for 'suspicion' to be "firmly grounded and targeted on specific facts" or based on "reasonable grounds", the fact that 'suspicion' has arisen must be open to proof, since to allow the defence of a suspicion of money laundering without any challenge would "in effect, be giving carte blanche to every bank to decline to execute their customer's instructions without any court investigation."⁵⁶ The judgment delivered by Lord Justice Longmore highlights that the court appreciated that POCA 2002 has placed banks in an "unenviable position", balancing the threat of criminal sanction against the threat of civil action by their clients. Nevertheless, Lord Justice Longmore emphasised at paragraph 32 that:

⁵¹ Marshall, P. (2010). 'Does Shah v HSBC Private Bank Ltd Make the Anti-money Laundering Consent Regime Unworkable?', *Butterworth Journal of International Banking and Financial Law*, 25 (5), pp. 287-290. For further discussion of the interplay between the subjective and objective tests present in POCA 2002 s330, see Swinton, K. (2007). 'When Do You Suspect it is Reasonable to Disclose?', *Scottish Law Gazette*, 75 (2), pp. 52-54.

⁵² POCA 2002 s328(2)(a) and s329(2)(a).

⁵³ POCA 2002 s333A.

⁵⁴ [2010] EWCA Civ 31.

⁵⁵ [2007] 1 WLR 303.

⁵⁶ [2010] EWCA Civ 31 para 30.

it cannot be right that proper litigation should be summarily dismissed without appropriate inquiry of any kind. The normal procedures of the court are not to be side-stepped merely because Parliament has enacted stringent measures to inhibit the notorious evil of money-laundering, unless there is express statutory provision to that effect.

This makes it abundantly clear that the court will not insulate the regulated sector from challenge simply because they have been given a statutory duty to assist in tackling money laundering. If they were to be afforded such privilege, the court would expect this to be specifically included in the legislative provision. Building on *R v Da Silva*,⁵⁷ this case emphasised the potential for actions for damages against regulated institutions where SARs have been made resulting in a delay in the execution of clients' instructions. While the Court acknowledges that these institutions are in a difficult position, it is emphasised that the burden remains theirs to carry. Nevertheless, rather than this case alarming the regulated sector, it should provide additional impetus to engage with a 'risk-based' approach establishing appropriate practices and procedures. In doing so, members of the regulated sector will not only be meeting their statutory obligations, but they will be arming themselves with sufficient evidence to rebut civil claims from clients.

The point has yet to receive judicial attention in Scotland. However, looking in particular to the case of *Mohammad Ahmad v HMA*,⁵⁸ also known as the 'Makkah Travel case', it appears that the Scottish courts are likely to follow the decision in *Shah v HSBC Private Bank Ltd*⁵⁹ (should it be brought to their attention). This case was a criminal appeal against conviction on a number of counts, including a failure to make a disclosure contrary to s330 POCA 2002. In this case, Mr Ahmad has been engaged in a business that is part of the regulated sector, Makkah Travel Ltd. The business acted as a travel agent and also as a money transmission bureau, administering transfers of money from Asian clients employed in the UK to family members in Pakistan. It came to the attention of HM Customs that there were some misgivings as to the legitimacy of the company's business. It was when cash was paid into the bank by Makkah Travel that the bank reported suspicious activity. No reports had been made by Makkah Travel in relation to the funds they had received or the transactions that they were being requested to implement. HM Customs consequently set up a surveillance operation, which founded the Crown's original case. It appeared that the accused had received a large amount of cash delivered in holdalls on numerous occasions from a Mr Gurie (who was a co-accused in respect of other charges). Mr Gurie was later acquitted on all charges. It was argued for the appellant that a proper construction of s330 required the Crown to prove that the money laundering allegedly known or suspected was indeed taking place, and since Mr Guthrie was acquitted it would be inconsistent for the jury to return a verdict which relied on the appellant's apparent failure to report activity which had, in reality, been found not to have taken place. However, the Court rejected this argument, explaining that it was based on a misunderstanding of the relevant section. Lord Kingarth further explained that s330(2) did not state that money laundering must be taking place for suspicion to be raised, rather "[a]s a matter of language it is obvious that a person may suspect that something is taking place, albeit it later turns out that his suspicion is ill-founded."⁶⁰ The emphasis here appears to lie firmly on the regulated institution to report any suspicious activity at the first opportunity. Lord Kingarth highlights that the purpose of the section is to prevent money laundering and to assist investigatory authorities, not to encourage those in the regulated sector to undertake the investigation themselves.

⁵⁷ [2007] 1 WLR 303.

⁵⁸ [2009] HCJAC 60(HCJ).

⁵⁹ [2010] EWCA Civ 31.

⁶⁰ [2009] HCJAC 60(HCJ) para 30.

While this case deals with the obligation for institutions to submit a SAR report in the first instance, the *Shah* case deals with duties owed to the client in respect of such a report once lodged. These cases illustrate the potentially conflicting interests that the regulated sector is seeking to balance. Both cases focus on the nature of the 'suspicion', agreeing that, while it may be necessary to found suspicion on relevant facts, it is not necessary to prove that a criminal act has taken place. It seems likely that, should an action for damages be raised in Scotland where a defence of lodging a SAR is put forward, the court would follow *Shah*. They would compel the regulated institution to evidence their 'suspicion' but not go so far as to demand that they prove that such suspicion was 'well-founded'.

Conclusion

It has been argued that there is a need for a re-conceptualisation of the 'private police' to accommodate the role of the regulated sector in the AML framework. However, it is acknowledged that further research is required into the role of professional bodies as supervisory authorities under MLR 2007 to fully explore where the line can be drawn between public and private police. Nevertheless, it has been demonstrated that the implementation of AML measures by the regulated sector increases the amount of intelligence available to policing agencies and thereby assists the public police in making appropriate operational choices. By making an initial SAR, the regulated sector is proactively driving policing investigation. Similarly, by supplying further information to the public police, they are supporting the public police investigations reactively. The role of the regulated sector is utilised by the public police as they are fundamentally tied together in their collation and dissemination of intelligence in AML operations.

While it may be the case that the public police are able to force the hands of the regulated sector to co-operate through criminal sanctions under POCA 2002 and MLR 2007, it is equally or perhaps more significant that the public police rely on the regulated sector to highlight investigation potential and to collate such information that may become a significant intelligence resource retrospectively. While the regulated sector may be required to undertake activities characteristic of policing, they remain restrained by their responsibilities to private interests as was demonstrated in *Shah v HSBC Private Bank Ltd*.⁶¹ Since the regulated sector are given a degree of flexibility and are able to balance their own and client interests, this means that they remain 'private' police rather than being subsumed into the state directed public police. Accordingly, the academic literature must adapt its conceptualisation of the 'private police' to reflect the role of the regulated sector in the AML framework.

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⁶¹ [2010] EWCA Civ 31.

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